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# In the Supreme Court of the United States.

OCTOBER TERM, 1919.

THE UNITED STATES, PETITIONER,
*v.*
NATIONAL SURETY COMPANY.
} Nos. —.

**PETITION FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT, AND BRIEF IN SUPPORT THEREOF.**

The Solicitor General, on behalf of the United States, prays that writs of certiorari may issue to review two decrees of the Circuit Court of Appeals for the Eighth Circuit rendered in the above-entitled cause December 10, 1919, being No. 201, original, and No. 5362 in said court.

## THE FACTS.

On November 29, 1916, the Bald Eagle Mining Company, a corporation, was adjudged a bankrupt. The National Surety Company, respondent herein, on November 3, 1917, filed with the referee two claims for $3,000 and $150, respectively, which were allowed as general claims. The sums represented payments made by it as surety to the United States of the amounts of two bonds securing the performance of contracts of the mining company to furnish coal at Jefferson Barracks, Missouri, and to the United States

Arsenal at St. Louis, Missouri, respectively, which contracts the bankrupt failed to perform.

On December 12, 1917, the United States filed with the referee its claim for $9,912.84, representing the loss incurred by it, after deducting the $3,000 paid by the surety company on account of the first-named bond, by reason of the default in performing the Jefferson Barracks coal contract. The referee allowed the claim as filed and ordered that it be accorded priority over all other claims against the bankrupt, with the exception of taxes and wages.

The surety company on March 12, 1918, filed with the referee motions to amend its claims for $3,000 and $150, asserting that under Revised Statutes, section 3468, they were entitled to the same preference accorded that of the United States. Said motions were granted and the referee ordered that the claims of the surety company should share in the distribution of the assets of the insolvent *pro rata* with the claim of the Government. (The assets of the estate available for distribution after payment of administration expenses were insufficient to pay in full the claims of the United States and the surety company.)

Thereafter the Government filed petitions for a review of said orders by the District Court for the Eastern District of Missouri. Said District Court affirmed said referee's orders, and appeal was taken by the Government to the United States Circuit Court of Appeals for the Eighth Circuit (No. 5362). A petition was also filed therein for revision of the orders and judgment complained of.

(No. 201, original.) The Circuit Court of Appeals (Judge Hook dissenting) on December 10, 1919, affirmed the decree of the District Court.

### THE STATUTES INVOLVED.

The material part of section 3466, Revised Statutes, reads:

> Whenever any person indebted to the United States is insolvent, * * * the debts due to the United States shall be first satisfied; * * *

The pertinent portion of section 3468, Revised Statutes, is as follows:

> Whenever the principal in any bond given to the United States is insolvent, * * * and * * * any surety on the bond * * * pays to the United States the money due upon such bond, such surety * * * shall have the like priority for the recovery and receipt of the moneys out of the estate and effects of such insolvent * * * principal as is secured to the United States; * * *

### THE QUESTION INVOLVED.

Is a surety who has paid to the United States the full amount of his bond, which, however, is less than the amount due the Government from the principal, a bankrupt, entitled to share *pro rata* with it (the United States) in the distribution of the assets of the bankrupt debtor, or is the claim of the United States superior and entitled to priority of payment?

REASONS FOR THE ALLOWANCE OF THE WRIT.

It is urged that the writs of certiorari should issue for the following reasons:

(1) This is the first time that the question herein involved has ever been presented to this Honorable Court.

(2) The question herein, decided below adversely to the Government by a divided court, is one which will undoubtedly arise very frequently in the future owing to the large number of contracts into which the Government is entering with private parties and for which surety bonds are given to secure the faithful performance thereof, and its correct settlement is of the greatest importance to the public business.

Wherefore it is respectfully prayed that this petition for writs of certiorari be granted.

ALEX. C. KING,
*Solicitor General.*
T. J. SPELLACY,
*Assistant Attorney General.*

MARCH, 1920.

BRIEF IN SUPPORT OF THE PETITION.

FIRST.

**A surety is not subrogated to the rights of the United States against the insolvent debtor until the claim of the Government is satisfied in full.**

Revised Statutes, section 3466, quoted supra, is merely declaratory of the old common-law principle

that debts of the sovereign are paramount and entitled to priority of payment over claims of private creditors. While it is conceded that section 3466 has been modified by the Bankruptcy Act of 1898 (sec. 64) to the extent that debts due the United States other than for taxes are not now of the first rank (*Guarantee Title & Trust Company* v. *Title Guaranty & Surety Company*, 224 U. S. 152) but stand sixth in order of liquidation, they are nevertheless still preferred claims and superior to those of the general creditor; and so far as the merits of this case go section 3466 is in full force and effect.

The ancient prerogative of the sovereign mentioned above depended upon the principle which determined "a preference in favor of the Crown in all cases and touching all rights of what kind soever where the Crown's and the subject's rights concur and so come into competition." This principle has recently been declared by the Privy Council of England never to have been questioned as a rule of law since the days of Lord Coke and to be of universal application except in so far as it has been modified by the legislature. (*New South Wales Taxation Commission* v. *Palmer*, 1907, A. C. 179.)

The doctrine has long been recognized in our own country and is one of the fundamental principles in our system of law. As this court said in the case of *Dollar Savings Bank* v. *United States*, 19 Wall., 227, 239:

> It may be considered as settled that so much of the royal prerogatives as belonged to the

> King in his capacity of *parens patriae*, or universal trustee, enters as much into our political state as it does into the principles of the British Constitution.

Speaking of provisions of the acts of March 3, 1797, and March 2, 1799, substantially identical with the provisions of section 3466, Revised Statutes, this court said in *United States* v. *Bank of North Carolina*, 6 Peters, 29, 35:

> The same policy which governed in the case of the royal prerogative, may be clearly traced in these statutes; and as that policy has mainly a reference to the public good, there is no reason for giving them a strict and narrow interpretation.

To permit the surety company in the instant case to be subrogated *pro tanto* to the rights of the United States against the estate of the bankrupt would defeat the express declaration of section 3466 that the debts due to the United States shall be first satisfied out of the assets of an insolvent estate. If the surety were so subrogated as to be placed upon a footing of equality with the United States, since the assets of the bankrupt's estate are insufficient to pay both claims in full the United States would suffer a reduction in the amount it would be entitled to in the distribution of such assets. To illustrate: In this case the assets of the bankrupt are $8,253.36. The claim of the United States is $9,912.84; that of the surety is $3,150. If the surety company is permitted to share *pro rata* in the distribution of the assets, it

will receive $1,990.23, to the loss and prejudice of the United States. To sustain the claim of the surety company is, therefore, not only contrary to the express declaration of Revised Statutes, section 3466, declaratory of the common law principle of the superiority of the sovereign's debts, but also of the well-settled equitable doctrine that the debt owing to the creditor must be satisfied in full before the surety can make any claim of subrogation to the rights and remedies of such creditor. As was stated in the case of *Receivers of New Jersey Midland Railway Company* v. *Wortendyke*, 27 N. J. Eq. 658, 661:

> The right of subrogation can not be enforced until the whole debt is paid; and until the creditor be wholly satisfied, there ought and can not be any interference with his rights or his securities, which might, even by bare possibility, prejudice or embarrass him in any way in the collection of the residue of his claim.

In the case of *Willingham* v. *Ohio Valley Banking & Trust Co.*, 22 Ky. Law Rep. 158, 56 S. W. 706, it was held that where a debtor pledged policies of life insurance to secure several debts which he owed the pledgee, a surety on one of the debts who had made payment thereof is not entitled to any part of the collateral security until all of the debts are paid, in the absence of agreement that each of the debts was to receive its *pro rata* of the security.

SECOND.

**The right of a surety to be subrogated to the priority of his creditor is a right which exists against all creditors of the principal debtor** *other than the obligee of the surety.*

Just as Revised Statutes, section 3466, is a statutory reenactment of the common law prerogative, so the above-quoted portion of Revised Statutes, section 3468, is a reenactment of the equitable rule of subrogation recognized in the law of principal and surety which also declared that a surety who has paid the debt of his principal to the sovereign is entitled to the sovereign's priority in the administration of his principal's estate. (*Manisty* v. *Church*, 39 Ch. D., 174; *Orem's Executrix* v. *Wrightson*, 51 Md., 34; *Richeson* v. *Crawford*, 94 Ill., 165; *In re Ryder*, 110 U. S., 729, 733.) The section should be construed in the light of the recognized principle that subrogation does not prevail against the creditor of the surety as to an unpaid part of the debt secured by the surety's obligation. As has been contended, under this section so construed a surety is not entitled to be subrogated to the rights of the creditor against the principal debtor until the creditor has been paid in full the debt on which the surety is liable in part, and this rule applies though the surety has paid all that he has agreed to pay. (*United States Fidelity & Guarantee Company* v. *United States Bank & Trust Company*, 228 Fed., 448.) As stated in Sheldon on Subrogation (2d ed.), section 127:

> Even if a surety is liable for only a part of the debt, and pays that part for which he is liable, he can not be subrogated to the securities held by the creditor for the debt until the whole demand of the creditor is satisfied.

The reason for this rule is that subrogation is a creature of equity and will never be allowed to the prejudice of the creditor. To hold otherwise is to defeat one of the objects of calling for a surety, i. e., to further secure the debt. That the United States would be prejudiced in the instant case if the surety company were subrogated to its rights has been hereinbefore demonstrated.

THIRD.

**Sections 3466 and 3468, Revised Statutes, are in pari materia and must, if possible, be construed so as not to conflict with each other.**

To sustain its claim that it should be allowed to share in the distribution of the bankrupt estate *pro rata* with the Government, the surety company relies upon Revised Statutes, section 3468, quoted supra, providing that in case of the insolvency of the principal on a bond given to the United States, the surety paying it shall have the like priority for the recovery of the moneys out of the estate of the bankrupt accorded the United States. The construction put upon that section by the surety company and the court below brings it squarely in conflict with section 3466, Revised Statutes. The latter section was originally enacted as section 5 of the act

of March 3, 1797 (1 Stat. 512, 515), the material part of which reads as follows:

> That where any revenue officer, or other person hereafter becoming indebted to the United States, by bond or otherwise, shall become insolvent, * * * the debt due to the United States shall be first satisfied, * * *

The section was reenacted as ~~part~~ of section 65 of the act of March 2, 1799 (1 Stat. 627, 676), and reads as follows therein:

> and in all cases of insolvency, * * * the debt or debts due to the United States, on any such bond or bonds (for payment of duties), shall first be satisfied; * * *

To section 65 was added as a proviso the provisions which were later enacted as Revised Statutes, section 3468. Said proviso reads as follows:

> *And provided also*, that if the principal in any bond, which shall be given to the United States for duties on goods, wares or merchandise imported, or other penalty, either by himself, his factor, agent, or other person for him, shall be insolvent, * * * and * * * any surety on the said bond or bonds, or the executors, administrators, or assignees of such surety shall pay to the United States the money due upon such bond or bonds, such surety, his or her executors, administrators or assignees, shall have and enjoy the like advantage, priority or preference for the recovery and receipt of the said moneys out of the estate and effects of such insolvent, * * *

> as are reserved and secured to the United States; * * *

Sections 3466 and 3468 are therefore in *pari materia* and must, if possible, be construed so as not to conflict with each other. As was stated by Mr. Justice Field in *Chicago, Milwaukee & St. Paul Rwy. Co.* v. *United States*, 127 U. S. 406, 409:

> Where there are two acts or provisions of law relating to the same subject, effect is to be given to both, if that be practicable.

The language of Revised Statutes, section 3468, would have to be very clear to justify this court in holding that it takes away the sovereign's prerogative of prior payment of its debts accorded by section 3466, declaratory of the ancient common law rule. A repeal of sovereign prerogative rights by implication is not favored. They can be taken away only by express words. *In re the Will of Wi Matua* 1908, A. C. 448.

FOURTH.

**The construction of section 3468, Revised Statutes, contended for by the Government is the only one which will give full effect to the provisions of that section as well as section 3466, Revised Statutes.**

Section 3468 gives the surety only a "like priority" as the United States would have. That priority is one over other creditors. The section does not attempt to confer upon the surety a preference over the Government whose debt it has guaranteed in whole or in part. The language of the statute is satisfied if the surety is given priority after all claims

of the United States have been paid. It does not either expressly or by implication give the surety the right to be subrogated to the claims of the United States so as to defeat its claim to prior payment.

The principle of construction here contended for by the Government has been adopted in the somewhat analogous case of *Robertson* v. *Trigg's Administrator*, 32 Grattan 76. The court there held that sureties of a United States collector, who had made default and died insolvent, were entitled under Revised Statutes, section 3468, to be subrogated to the right of priority of the United States in the payment of a debt, when they had paid it, as against the estate of a cosurety who had died before the insolvency of the collector. It was argued that because the statute made no express provision for the substitution of a surety to the rights of the creditor against a cosurety, it was intended to exclude such substitution, but the court held that the rule of substitution for the purpose of enforcing contribution between the sureties was too well established in equity to be set aside by implication of less force than an express statutory denial of the remedy. So here, the limitation upon the rule of subrogation of the surety to the creditor's rights against the principal debtor that such subrogation will never be allowed to the prejudice of the creditor is so well established that it should not be regarded as abolished unless the intention so to do is clearly expressed.

If section 3468 is construed as establishing a statutory right of a nature similar to the equitable

doctrine of subrogation (as the Government contends it should be), then clearly the court below erred in holding that the surety was entitled under the circumstances of this case to be subrogated *pro tanto* to the rights of the United States against the mining company, not only as to other creditors, but also as to the United States.

### CONCLUSION.

Wherefore it is respectfully submitted that the petition for writs of certiorari to review the decision of the United States Circuit Court of Appeals for the Eighth Circuit should be granted.

ALEX C. KING,
*Solicitor General.*
T. J. SPELLACY,
*Assistant Attorney General.*

MARCH, 1920.

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IN THE

# SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1919.

THE UNITED STATES, *Petitioner,*

v.

NATIONAL SURETY COMPANY,

Petition for Writs of Certiorari to the United States Circuit Court of Appeals for the Eighth Circuit.

## BRIEF FOR NATIONAL SURETY COMPANY IN OPPOSITION.

SAMUEL W. FORDYCE,
JOHN H. HOLLIDAY,
THOMAS W. WHITE,
Solicitors for National Surety Company.

St. Louis Law Printing Co., Ninth and Walnut Sts. Main 1848.

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## BRIEF FOR NATIONAL SURETY COMPANY IN OPPOSITION.

## STATEMENT.

Counsel for petitioner have substantially stated the facts. There are several matters, however, that we wish to add.

On October 9th, 1917, the United States received full payment of the three thousand dollar bond exe-

cuted by the National Surety Company. The release and receipt executed in connection with said bond is in part as follows:

> "Now, therefore, for and in consideration of the sum of three thousand dollars ($3,000.00) in hand paid to the party of the first part by the party of the second part, receipt whereof is hereby acknowledged by the party of the first part, the party of the first part acknowledges the said payment in full settlement and satisfaction of all claims, charges, damages and controversies existing or which may in the future exist or arise out of said bond above set forth, and discharges and agrees forever to hold harmless the said party of the second part from any and all liability, judgment or damages arising or which in the future may arise out of said bond."

On December 30th, 1916, the United States received one hundred and fifty dollars in full payment and satisfaction of the other bond executed by the National Surety Company. The release and receipt of the United States is substantially the same as the release and receipt executed in connection with the three thousand dollar bond.

**The Question Involved.**

The question involved is: If a surety on a bond to the United States pays the full amount of the bond and the United States receipts for same and acknowl-

edges full settlement and satisfaction, is the surety entitled, under Section 3468, Revised Statutes, to like priority to that of the United States for the recovery of said money paid on said bond, and does this like priority entitle the surety to a *pro rata* distribution with the United States of the assets of a bankrupt debtor, in case the full amount of the bond is less than the amount due the Government from the principal, the bankrupt debtor?

# ARGUMENT.

**The National Surety Company is entitled to like priority as is secured to the United States, because it has paid in full to the United States the bonds on which it was surety for the bankrupt.**

The sections of the Revised Statutes of the United States involved in this case are Section 3466 and Section 3468, and they are as follows:

> Section 3466, R. S.: "Whenever any person indebted to the United States is insolvent, or whenever the estate of any deceased debtor, in the hands of executors or administrators, is insufficient to pay all the debts due from the deceased, the debts due to the United States shall be first satisfied; and the priority hereby established shall extend as well to cases in which a debtor, not having sufficient property to pay all his debts, makes a voluntary assignment thereof, or in which the estate and effects of an absconding, concealed, or absent debtor are attached by process of law, as to cases in which an act of bankruptcy is committed."
>
> Section 3468, R. S.: "Whenever the principal in any bond given to the United States is insolvent or whenever, such principal being deceased, his estate and effects which come to the

hands of his executor, administrator, or assignee, are insufficient for the payment of his debts, and, in either of such cases, any surety on the bond, or the executor, administrator, or assignee of such surety pays to the United States the money due upon such bond, such surety, his executor, administrator, or assignee, shall have the like priority for the recovery and receipt of the moneys out of the estate and effects of such insolvent or deceased principal as is secured to the United States; and may bring and maintain a suit upon the bond, in law or equity, in his own name, for the recovery of all moneys paid thereon" (2 Fed. Stat. Ann. [2nd Ed.], 216, 6 U. S. Compiled Stats., p. 7420).

The argument of petitioner is based entirely on the theory of common-law subrogation. It is asserted by petitioner that Section 3468 is merely declaratory of the common law, that it is subject to the same limitations as exist at common law, that one of these limitations is that the creditor to whom both the principal and his surety are debtors, must be first paid in full before the surety is entitled to enforce his right of subrogation.

Our answer to this is contained in the very wording of the statute. Counsel for petitioner have entirely overlooked the wording of this statute. The priority arises to the surety when it pays in full "the money due upon such bond" and not when the creditor is paid in full.

We are of the opinion that Section 3468, R. S., was enacted for a definite specific purpose and was not intended to be declaratory of the common law. Had Congress intended to make the statute declaratory of the common-law subrogation, it would not have been limited to insolvent principals. The right of subrogation arises at common law whether the principal is solvent or insolvent. The section did not attempt to cover all cases, but simply to cover the case of an insolvent principal, where a surety pays all of the money due upon the *bonds* which it has executed. The statute gives the "*right of priority*" to the surety for "*the moneys*" paid on the surety's "*bond.*"

In the case of the United States v. Heaton, 128 Fed. 414 (C. C. A., 3rd Circuit), the Court approved this language used by the Circuit Court in deciding the case below:

> "The United States has no priority against a surety, for the reason that no statute has given it such a privileged position, while it has priority against an insolvent principal for the analogous reason that Congress has seen fit so to enact. The right of a surety, after he has paid the *money due upon his bond* to the United States, to be preferred in the distribution of his insolvent principal's estate, does not depend at all upon the answer to the question whether the United States has previously had priority against the

surety, *but rests solely upon the language of Section 3468, which expresses the legislative will upon the subject. It is this section that is the source of the surety's right, and I think its true construction gives priority for so much, and no more of the Government's claim as the surety may have beeen obliged to pay* by legal proceedings, or may have paid voluntarily, *in discharge of his obligation upon the bonds.*" (Italics are ours.)

In the case of United States v. Ryder, 110 U. S. 729, 28 Lawyer's Edition 308, *l. c.* 311, the Court said that section 3468 was substantially a reproduction of the proviso of the Act to Regulate the Collection of Custom Duties, approved March 2, 1799 (1 Stat., at L., 676). The Court said:

"The only difference between section 3468 of the Revised Statutes and this proviso is, that the latter in terms relates to bonds given for duties, whilst the former uses the more general terms, 'whenever the principal in any *bond given to the United States* is insolvent, etc.' If it was intended by Congress to enlarge the scope of the section so as to include other bonds than those given for duties, as seems to be the necessary inference from the language, still, it is restricted to '*bonds*'; the words are 'whenever the principal in any *bond* given to the United States is insolvent, etc.', and any 'surety on the *bond*' pays *the money due upon 'such bond,'* such

surety shall have the like priority, etc., and may bring and maintain a suit upon '*bond*' in his own name, *etc. This cautious phrascology*, so carefully avoiding any general words of enlargement beyond the article of '*bonds*' alone, seems to imply that, in extending the peculiar privileges given to sureties, it was only intended to do so in reference to obligations of the same general character with those referred to in the original act, that is to say, bonds conditioned for the payment of money, or, at most, to embrace, besides, those conditioned for the performance of some civil duty, such as the faithful discharge of the duties of an office, etc."

In the case of Hunter v. United States, 5 Peters 173, 8 Lawyers' Edition 86, Hunter was the assignee of Archibald and Frederick Crary. Jacob Smith had, as surety in a custom house bond, been compelled to pay to the United States, for the Crarys, the sum of $2,125.00. This payment was made in 1808. In 1809 the United States obtained judgment against Smith on another bond and Smith went into insolvency. The United States claimed priority in the Crary estate, against the other Crary creditors, on the ground that Smith, having paid a bond to the United States, was entitled to priority over the other Crary creditors. The Supreme Court of the United States sustained the priority.

The holding of the Court is to the effect that under the statutes of the United States, the surety who

pays to the United States the amount of a bond, is entitled to priority over other creditors in an insolvent estate. This is peculiarly emphasized in this case, for the reason that the Government established its claim to the assets of an insolvent estate by claiming through one who had paid to the Government the amount of the surety bond.

From the above authorities and from the express language of section 3468, it is apparent that priority arises to the surety when the surety pays *"the money due upon such bond."* The statute does not provide that priority shall arise to the surety when the surety has paid *all the claims of the Government* against a bankrupt or insolvent estate. Had Congress intended that the United States should be paid in full for *all claims* which it had against a bankrupt or an insolvent, before a surety was entitled to priority after paying the full amount of its bond, suitable wording could have been used to express this thought.

In this connection, we call the Court's attention to the fact that in section 3466, the words used are *"all debts due"* and *"the debts due* to the United States," but the words used in section 3468 are, "such surety pays to the United States *the money due upon such bond"* and "such surety shall have the like priority for the recovery and receipt of *the moneys* out of the estate and effects of such insolvent" and the surety "may bring and maintain a

suit upon the bond * * * for the recovery of *all moneys paid* thereon". Under section 3468, the surety pays *the moneys* due on the bond and is given the like priority to the United States to recover *the moneys* paid on the bond and expressly states that the surety may recover *"all moneys paid thereon";* the words *"all moneys"* means "any moneys" or "whatever moneys," or, as held by the Supreme Court in United States v. Heaton, *supra*, "Its true construction gives priority for so much, and no more, of the Government's claim as the surety may have been obliged to pay by legal proceedings or may have voluntarily paid, in discharge of his obligations upon his bond."

The Supreme Court stated in United States v. Ryder, *supra*, that the wording of the statute is "cautious phraseology." Congress, in other words, not only meant what it said, but said what it meant. The Government in its brief seeks to insert an exception in this statute and such an exception as is in contradiction of the express phraseology so "cautiously" used. Had Congress intended an exception, it could have easily added a proviso, or the wording of the statute itself could have been changed, so that the priority of the surety would not arise on its paying "the moneys due on such bond," but on its paying "all debts due to the United States from such insolvent or deceased principal."

The surety bases its right entirely upon that statute, and under it the surety is entitled to the same priority as the United States Government is, in an insolvent estate, *when the money due upon a bond is paid.*

In the releases and receipts signed by the United States at the time it was paid in full the amounts of the bonds, provide as follows:

> "This release and receipt is in full payment and satisfaction of all claims whatsoever on said *bond*, etc."

The Government having been paid in full by the surety company, the surety is entitled to the same priority that the Government has in the insolvent estate.

The authorities cited by opposing counsel are not in point. They are cases arising out of subrogation at common law, and not under section 3468, R. S. Section 3468 was not intended to cover all the various situations arising in common-law subrogation. The purpose of the statute is clearly limited to an insolvent estate and to payments made by sureties on Government bonds, and awards priority where the surety pays the full amount of the *bond*. There is no requirement under the statute that the surety shall pay *all the debts* owing by an insolvent estate to the Government, before the surety is entitled to priority.

We have read carefully the decisions cited in the brief of petitioner. These cases do not hold that the surety company is not entitled to priority where the surety has paid the full amount of the *bond* to the Government. Only one of the cases involve Government bonds, and in this case the Government was paid in full of its debt and the surety had also discharged the full amount of the bond. There is no case cited by the Government in their brief where a surety on a Government bond has paid the full amount of the bond, and the Government had not been paid in full of its debt, and these are the facts in the case at bar.

The reference to section 3468 in the case of Robertson v. Trigg's Administrator, 32 Grattan 76, is wholly *obiter*, for no claim of a surety was sought under section 3468.

In the cases of United States Fidelity and Guaranty Co. v. United States Bank and Trust Co., 228 Fed. 448, and Columbia Fidelity and Trust Company v. Kentucky Union Railway Co., 60 Fed. 794, the Court's decision is based entirely on common-law subrogation and not upon section 3468, no Federal bond was involved and the Federal statute is not even mentioned in the opinions.

The Government's brief contends that the prerogative of sovereignty in priority of debts to it, is such that it cannot be taken away except by express language. We contend express language has been used

in section 3468 sufficient to give to the surety the right of priority, when it has paid the *bond* in full.

When the statute was enacted, the common law of subrogation was well understood and the prerogative of the Government to priority was also well understood. Having both of these principles in mind, Congress of the United States provided in clear and unambiguous language, that when "such surety pays to the United States *the money due upon such bond,* such surety shall have like priority for the recovery of *the moneys.*"

We do not know how the idea of priority of the surety could have been more clearly expressed. The meaning of section 3468 is shown in the quotations above set forth, from the cases of United States v. Heaton, 128 Fed. 414, *l. c.* 417 (C. C. A., 3rd Cir.), and United States v. Ryder, 110 U. S. 729, 28 Lawyer's Edition 308, *l. c.* 311.

The Government's brief contends that if priority is allowed to the surety in this case, the Government will lose some money. The surety in this case declines to assume the responsibility of the Government's losing the money. The surety has paid in full the bonds executed to the Government, and, as stated by the District Court in deciding this case, the bonds were "paid promptly."

The Government could have very easily secured payment of its loss in full by requiring a larger bond.

The Government itself fixed the size of the bond; the Surety Company had no decision in the matter. The bond was arranged between the Government and the contractor. Congress evidently presumed that the officers of the Government would ask for a bond that would fully protect it; hence provided that when the bond was paid in full, the surety's priority was substituted for the priority of the Government.

There is no way to protect the Government if it insists on procuring such a small bond. If the Government had only required a $100.00 bond for a $3,000.00 contract, the Government would simply be running a chance in having the contractor fail and receiving only $100.00 from the surety.

The Government contends that if it had chosen to file its claim in bankruptcy for the full amount of its loss, and had been paid such an amount as it could have secured as a preferred claimant, it could have then proceeded on the bonds in question, and the Surety Company would have no defense.

The answer to this contention is that no such case is presented by the record. The Surety Company paid in full the amount of the bonds and the Government receipted for the money in full and afterwards the Government then proceeded against the bankrupt's estate. The Government having proceeded against the Surety Company first on the bonds, the Surety Company is entitled to the same priority as the Govern-

ment against the insolvent estate. Even if the Government had proceeded against the insolvent estate before proceeding against the surety, the surety could have protected its priority by tendering to the United States the amount of the bonds, and a refusal by the Government to accept the tender would have released the surety.

This not only destroys the argument of the Government that it could have secured the assets of the bankrupt estate and then have proceeded against the surety, but shows definitely that the proper construction of section 3468, giving the surety "like priority" with the Government, is fully protected, and that the construction contended for by us is the correct one. If the law is as contended for by the Government, it is surprising that the Government should have first made demand on the surety company for the full amount of the bonds and actually received from the Surety Company full payment of the bonds, signing a receipt and release for same, and then afterwards filed the claims in the bankrupt estate. The very action of the Government in collecting in full the amount of the bonds before filing the claim in the bankrupt estate shows that the Government understood that the surety's priority would be protected in all events. The course of the Government is not in accordance with its present contention.

The Government contends that under its construction of section 3468, the United States should receive the entire amount of the assets of the estate of the bankrupt mining company, leaving nothing for the surety company. The position of the Government is, therefore, that the proper construction of section 3468 is entirely dependent upon the amount of the assets of the bankrupt estate. Our contention is that the meaning of the statute is not dependent upon the amount of the assets of the bankrupt estate, and that the words "like priority" mean that the surety has the same priority of the Government itself.

It would frequently be impossible to tell until after the time for filing the claims had expired whether or not there would be enough money to pay the Government's claims in full and still give the Surety Company a sufficient dividend to reimburse it.

The construction which the Government places upon section 3468 is apparently this: If the bankrupt estate has sufficient to pay the United States' claim in full, after the Surety Company has paid its bond in full, then the Surety Company is entitled to "like priority," but if there is not sufficient assets to pay the Government's claim and the surety's also, then the words "like priority" have no meaning. As we view the express wording of the statute, the words "like priority" mean exactly what they say, whatever the amount of the bankrupt estate. The statute

provides that the Surety Company and the United States have "like priority," so far as their participation in the bankrupt estate is concerned, after the payment by the surety of the full amount of the bond. The Surety Company and the United States must, therefore, participate *pro rata* in the assets of the bankrupt estate.

The whole argument of the Government should be addressed to the Congress and not to this Court. Section 3466 of Revised Statutes was in effect before the enactment of section 3468. It is evident, therefore, that Congress, representing the sovereign, intended to give the surety the priority which we are contending for. If the Government thinks that Congress has overlooked the possibility of the Government's accepting bonds which are not sufficient protection to Government contracts, then this is a matter for the Congress.

We are forced to the conclusion that the petition should be denied.

Respectfully submitted,

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## AUTHORITIES CITED.

THE STATUTES.

# In the Supreme Court of the United States.

OCTOBER TERM, 1920.

THE UNITED STATES, PETITIONER, v. NATIONAL SURETY COMPANY. } Nos. 271 and 272.

*ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT.*

## BRIEF FOR THE PETITIONER.

### STATEMENT OF THE CASE.

This case comes here on a writ of certiorari to the United States Circuit Court of Appeals for the Eighth Circuit granted herein May 6, 1920 (R. 51[1]) to review the decree of said Circuit Court of Appeals entered December 10, 1919 (R. 50) affirming the order and decree of the District Court of the United States for the Eastern District of Missouri, entered on December 31, 1918, in the matter of Bald Eagle Mining Company, a corporation, bankrupt (R. 43).

### THE FACTS.

In June, 1916, the Bald Eagle Mining Company entered into two contracts with the United States Government to furnish to it certain coal at certain

[1] All references are to the record in No. 271.

prices and within a certain time. To secure the performance of these contracts, the Mining Company executed two bonds, one for $3,000 and one for $150, with the National Surety Company as surety. The Mining Company failed to perform the contracts and the United States was compelled to buy in the open market the amount of coal contracted for by it. This caused a loss to the United States of about $13,000.

On November 29, 1916, the Mining Company was adjudicated a bankrupt. On November 3, 1917, the National Surety Company, respondent herein, having paid the United States $3,150, the amount of the bonds, filed with the referee in bankruptcy two claims against the bankrupt for $3,000 and $150, respectively (R. 20, 30), which were allowed on said date as general claims. On December 12, 1917, the United States filed with said referee its claim in the sum of $9,912.84, representing the loss incurred by it after deducting the $3,150 paid it by the surety company, and on the same day said referee made an order allowing said claim and directed that it be accorded priority over all other claims except those for wages and taxes (R. 6). The Mining Company's assets were not sufficient to pay in full the claims of both the United States and the Surety Company (R. 10).

On March 12, 1918, more than one year subsequent to the date of adjudication, the Surety Company moved for leave to amend its claims and to have them allowed as preferred claims of the same class

as that of the United States (R. 8, 9). These motions were granted by the referee (R. 38, 39). From the judgment of the District Court approving and confirming this order (R. 43) the United States appealed to the Circuit Court of Appeals for the Eighth Circuit. It also filed in that court a petition to revise the order of the District Court (R. 1). The Circuit Court of Appeals (Judge Hook dissenting) affirmed the judgment of the District Court.

THE STATUTES.

The construction of the following sections of the Revised Statutes is necessary to a determination of the issues involved in this case:

> Section 3466: Whenever any person indebted to the United States is insolvent, or whenever the estate of any deceased debtor, in the hands of executors or administrators, is insufficient to pay all the debts due from the deceased, the debts due to the United States shall be first satisfied; and the priority hereby established shall extend as well to cases in which a debtor, not having sufficient property to pay all his debts, makes a voluntary assignment thereof, or in which the estate and effects of an absconding, concealed, or absent debtor are attached by process of law, as to cases in which an act of bankruptcy is committed.
>
> Section 3468: Whenever the principal in any bond given to the United States is insolvent, or whenever, such principal being deceased, his estate and effects which come to the hands of his executor, administrator, or

> assignee are insufficient for the payment of his debts, and, in either of such cases, any surety on the bond, or the executor, administrator, or assignee of such surety pays to the United States the money due upon such bond, such surety, his executor, administrator, or assignee shall have the like priority for the recovery and receipt of the moneys out of the estate and effects of such insolvent or deceased principal as is secured to the United States, and may bring and maintain a suit upon the bond, in law or equity, in his own name, for the recovery of all moneys paid thereon.

THE CONTENTIONS OF THE PARTIES.

Respondent, while not disputing that at common law it would not be entitled to be subrogated to the rights of the sovereign against the bankrupt until the latter's obligation to the former had been paid in full, contends that the law has been changed by Revised Statutes, section 3468, and that under that statute the surety, having paid the Government the amount due on the bond executed by it, though less than the amount due from the principal debtor, is subrogated *pro tanto* to the rights of the United States against such principal debtor.

The Government, on the other hand, contends that Revised Statutes, section 3468, does not change the common law, but is merely declaratory of it; that only by so construing section 3468 can full effect be given to all the provisions of that section as well as of section 3466 and a conflict between the two, which are in *pari materia*, be avoided.

ARGUMENT.

## I.

**At common law a surety is not subrogated to the rights of the sovereign against the principal debtor until the claim of the former has been satisfied in full.**

In this case petitioner and respondent set up conflicting claims to the assets of a bankrupt corporation. The Government's claim is for $9,912.84; that of the surety is for $3,150. The assets of the bankrupt are $8,253.36. If the surety is subrogated *pro tanto* to the rights of the United States against the estate of the bankrupt, it will receive $1,990.23 and the sum the Government will receive in satisfaction of its claim against the bankrupt will be diminished by that amount. To permit the surety to profit in this manner at the expense of the United States is clearly contrary to several well-established principles of law.

First. The right of a surety to be subrogated to the rights of the creditor against the principal debtor is the creature of equity. It is elementary that such subrogation will never be permitted to the prejudice of the creditor. Otherwise, the object of calling for a surety, i. e., to further secure payment of the debt, would be defeated.

Hence it is well established that a surety is not entitled to be subrogated to the rights of the creditor against the principal debtor until the latter's debt to the former has been paid in full, and this rule

applies though the surety was liable for only part of the debt and has paid that part. As stated in Sheldon on Subrogation, 2d Ed., section 127:

> Even if a surety is liable only for a part of the debt, and pays that part for which he is liable, he can not be subrogated to the securities held by the creditor for the debt, until the whole demand of the creditor is satisfied.

In *Peoples* v. *Peoples Brothers, Inc.*, 254 Fed. 489, it was held that the surety on a building contractor's bond, conditioned for the payment of claims for labor and material, which, on the contractor's insolvency, paid into court the amount of its obligation, which sum was, however, sufficent to pay only 65 per cent of the claims of creditors secured by the bond, was not entitled by subrogation to the amount paid by it until the claims for labor and material were paid in full. To the same effect see *United States Fidelity & Guaranty Company* v. *Union Bank & Trust Company*, 228 Fed. 448; *National Bank of Commerce* v. *Rockefeller*, 174 Fed. 22; *Wilcox* v. *Fairhaven Bank*, 7 Allen, 270; *Swan* v. *Patterson*, 7 Md. 164; *Willingham* v. *Ohio Valley Banking & Trust Company*, 22 Ky. Law Rep. 158.

Second. In this instance the creditor is the sovereign, and it is well settled that the debts of the sovereign are paramount and entitled to priority of payment over the claims of private creditors. Revised Statutes, section 3466, so far as material here, provides that "Whenever any person indebted to the United States is insolvent * * * the debts due

to the United States shall be first satisfied * * *." This statute is merely declaratory of the old common law principle just stated.

True, the statute limits the application of the principle to the circumstances therein set forth, that is, where the debtor is insolvent or has died leaving insufficient assets to pay all his debts, etc.; but it is, nevertheless, within its scope an application of the common law principle.

While it is conceded that section 3466 has been modified by the bankruptcy act of 1898 (sec. 64) to the extent that debts due the United States other than for taxes are not now of the first rank (*Guarantee Title & Trust Company* v. *Title Guaranty & Surety Company*, 224 U. S. 152) but stand sixth in order of liquidation, they are, nevertheless, still preferred claims and superior to those of the general creditor, and so far as the merits of this case go section 3466 is in full force and effect.

The ancient prerogative of the sovereign mentioned above itself depended upon the principle which determined "a preference in favor of the Crown in all cases and touching all rights of what kind soever where the Crown's and the subject's right concur and so come into competition." This principle has recently been declared by the Privy Council of England never to have been questioned as a rule of law since the days of Lord Coke and to be of universal application, except in so far as it has been modified by the legislature. (*New South Wales Taxation Commissioners* v. *Palmer*, 1907, A. C. 179.)

This prerogative right of the sovereign has long been recognized by the courts of this country and is one of the fundamental principles in our system of law. As this court said in the case of *Dollar Savings Bank* v. *United States*, 19 Wall., 227, 239:

> It may be considered as settled that so much of the royal prerogatives as belonged to the King in his capacity of *parens patriæ*, or universal trustee, enters as much into our political state as it does into the principles of the British Constitution.

Speaking of provisions of the acts of March 3, 1797, and March 2, 1799, substantially identical with the provisions of section 3466, Revised Statutes, this court said in *United States* v. *Bank of North Carolina*, 6 Peters, 29, 35:

> The same policy which governed in the case of the royal prerogative may be clearly traced in these statutes; and as that policy has mainly a reference to the public good, there is no reason for giving to them a strict and narrow interpretation.

It is clear, therefore, that both at common law and under the express provisions of Revised Statutes, section 3466, the surety can not share in the distribution of the bankrupt's assets until the claim of the United States has been satisfied in full.

## II.

**Revised Statutes, section 3468, does not change the common law, but is merely declaratory of it.**

Respondent does not dispute the correctness of the Government's contention as to the common law. It contends, however, that the common law has been changed by Revised Statutes, section 3468. This contention is based on the declaration of that statute that whenever "any surety on the bond * * * pays to the United States the money due upon such bond, such surety * * * shall have the like priority * * * as is secured to the United States." Respondent's contention, which was adopted by the majority of the Circuit Court of Appeals, is that the fact that the statute provides that the surety shall have the like priority as the United States whenever it pays the United States the money due upon its bond shows that the common law has been changed and that under the statute it is not a condition precedent to the surety's right of subrogation that the Government shall have been paid in full.

This contention is obviously unsound. Section 3468 is no more than a statutory declaration of the common law principle that a surety who has paid the debt of his principal to the sovereign is entitled to the sovereign's priority in the administration of his principal's estate. (*Manisty* v. *Churchill*, 39 Ch. D. 174; *Orem, Executrix* v. *Wrightson*, 51 Md. 34; *Richeson* v. *Crawford*, 94 Ill. 165; *United States* v. *Ryder*, 110

U. S. 729.) Under this section the surety is subrogated to the rights of the creditor against the principal debtor only if he would have had that right at common law.

This construction is the only one which will give full effect to the provisions of that section as well as of section 3466. Section 3468 gives the surety only a "like priority" as the United States would have. That priority is one over other private creditors. The section does not attempt to confer upon the surety a preference over the Government whose debt it has guaranteed in whole or in part. The language of the statute is satisfied if the surety is given priority after all claims of the United States have been paid. It does not, either expressly or by implication, give the surety the right to be subrogated to the claims of the United States when, as in the case at bar, the latter's claim to prior payment would be defeated and the surety would escape the full performance of its obligations.

To construe this section differently would be to bring it squarely in conflict with section 3466. The latter section was originally enacted as section 5 of the act of March 3, 1797 (1 Stat. 512, 515), the material part of which reads as follows:

> That where any revenue officer, or other person hereafter becoming indebted to the United States, by bond or otherwise, shall become insolvent, * * * the debt due to the United States shall be first satisfied, * * *.

That section was partly reenacted as a portion of section 65 of the act of March 2, 1799 (1 Stat. 627, 676), and reads as follows therein:

> and in all cases of insolvency, * * * the debt or debts due to the United States, on any such bond or bonds (for payment of duties), shall be first satisfied: * * *.

To section 65 was added as a proviso the provisions which were later enacted as Revised Statutes, section 3468. Said proviso reads as follows:

> *And provided also*, That if the principal in any bond which shall be given to the United States for duties on goods, wares, or merchandise imported, or other penalty, either by himself, his factor, agent, or other person for him, shall be insolvent, * * * and * * * any surety on the said bond or bonds, or the executors, administrators, or assignees of such surety shall pay to the United States the money due upon such bond or bonds, such surety, his or her executors, administrators, or assignees shall have and enjoy the like advantage, priority, or preference for the recovery and receipt of the said monies out of the estate and effects of such insolvent, * * * as are reserved and secured to the United States: * * *.

Sections 3466 and 3468 are derived from this section and are therefore in *pari materia*. They must, if possible, be construed so as not to conflict with each other. As was stated by Mr. Justice Field in *Chicago, Milwaukee & St. Paul Ry. Co.* v. *United States*, 127 U. S. 406, 409:

> When there are two acts or provisions of law relating to the same subject, effect is to be given to both, if that be practicable.

This court has held that Revised Statutes, section 3466, is not to be strictly or narrowly construed. *United States* v. *Bank of North Carolina*, 6 Peters 29, 35. The language of section 3468 would have to be very clear to justify this court in holding that it repeals to the extent contended for by the Surety Company the rule of the common law and section 3466, that the sovereign is entitled to priority in the payment of debts due it over those due a private creditor. A repeal of the sovereign's prerogative rights by implication is not favored. They can be taken away only by express words. In re the Will of Wi Matua, 1908, A. C. 448.

The principle of construction here contended for by the Government has been adopted in the somewhat analogous case of *Robertson* v. *Trigg's Administrator*, 32 Grattan 76. The court there held that sureties of a United States collector, who had made default and died insolvent, were entitled under Revised Statutes, section 3468, to be subrogated to the right of priority of the United States in the payment of a debt, when they had paid it, as against the estate of a cosurety who had died before the insolvency of the collector. It was argued that because the statute made no express provision for the substitution of a surety to the rights of the creditor against a cosurety, it was intended to exclude such substitution, but the court held that the rule of substitution for the purpose

of enforcing contribution between the sureties was too well established in equity to be set aside by implication of less force than an express statutory denial of the remedy. So here the limitation upon the rule of subrogation of the surety to the creditor's rights against the principal debtor that such subrogation will never be allowed to the prejudice of the creditor is so well established that it should not be regarded as abolished unless the intention so to do is clearly expressed.

It is said that this construction is unreasonable, because if so construed section 3468 confers no priority upon the surety unless he pays all of the debt or debts due from the bankrupt to the United States, and if he pays more than the amount he is obligated to pay he is a mere volunteer and not entitled to subrogation as to the excess.

That this is the consequence of adopting the Government's contention is true; but such is undoubtedly the law unless the common law has been modified by statute. And to construe section 3468 as modifying the common law is contrary to all the recognized canons of construction.

Besides, the consequence of adopting respondent's contention would be that the extent to which the Government could enforce satisfaction of its claim would depend upon whether it proceeded first against the surety or against the bankrupt, a result surely not contemplated by Congress. If the United States proceeded first against the bankrupt, all of his assets would have to be applied to the satisfaction of the

Government's claim and the surety would be liable to the Government for the unsatisfied balance of its claim, if any, without being able to recover the amount paid by it from the bankrupt. If, on the other hand, the Government proceeded first against the surety and proved the unsatisfied balance of its claim against the bankrupt estate of the principal debtor, the surety would be allowed to share pro rata in the distribution of his assets. A result so unreasonable must, if possible, be avoided.

If section 3468 is construed as establishing a statutory right of a nature similar to the equitable doctrine of subrogation (as the Government contends it should be), then clearly the court below erred in holding that the surety was entitled under the circumstances of this case to be subrogated *pro tanto* to the rights of the United States against the mining company not only as to other creditors, but also as to the United States.

## CONCLUSION.

Wherefore it is respectfully submitted that the decree of the Circuit Court of Appeals should be reversed and the cause remanded.

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*Assistant Attorney General.*
LEONARD B. ZEISLER,
*Special Assistant to the Attorney General.*

SEPTEMBER, 1920.

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## AUTHORITIES CITED.



## THE STATUTES.

IN THE

# SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1920.

THE UNITED STATES,
Petitioner,
v.
NATIONAL SURETY COMPANY.

Petition for Writs of Certiorari to the United States Circuit Court of Appeals for the Eighth Circuit.

## BRIEF FOR RESPONDENT, NATIONAL SURETY COMPANY.

## STATEMENT OF THE CASE.

Counsel for petitioner have substantially stated the facts. There are several matters, however, that we wish to add.

On October 9th, 1917, the United States received full payment of the three thousand dollar bond executed by the National Surety Company. The release and receipt (Rec., p. 34) executed in connection with said bond is in part as follows:

"Now, therefore, for and in consideration of the sum of three thousand dollars ($3,000.00) in hand paid to the party of the first part by the party of the second part, receipt whereof is hereby acknowledged by the party of the first part, the party of the first part acknowledges the said payment in full settlement and satisfaction of all claims, charges, damages and controversies existing or which may in the future exist or arise out of said bond above set forth, and discharges and agrees forever to hold harmless the said party of the second part from any and all liability, judgment or damages arising or which in the future may arise out of said bond."

On December 30th, 1916, the United States received one hundred and fifty dollars in full payment and satisfaction of the other bond executed by the National Surety Company. The release and receipt of the United States is substantially the same as the release and receipt executed in connection with the three thousand dollar bond (Rec., p. 36).

## The Question Involved.

The question involved may be thus stated:

Is the surety, who has paid to the United States the full amount of its bond, entitled under Section 3468, R. S., to "the like priority" of the United States over other creditors of the insolvent estate of the

principal, only when all the debts owing by the insolvent principal to the United States have been paid (as claimed by petitioner), or, "whenever the surety pays to the United States the money due upon such bond" (as stated in section 3468, and as contended for by respondent)?

# ARGUMENT.

**Under section 3468, a surety on a bond to the United States is entitled to like priority to the United States against the insolvent principal's estate "whenever the surety pays to the United States the money due upon such bond", and it is not necessary for the surety or the principal to pay all the debts due from the principal to the United States to entitle the surety to this "like priority".**

The pertinent parts of the sections of the Revised Statutes of the United States involved in this case are as follows:

> Section 3466, R. S.: "Whenever any person indebted to the United States is insolvent, or whenever the estate of any deceased debtor, in the hands of executors or administrators is insufficient to pay all the debts due from the deceased, the debts due to the United States shall be first satisfied; * * *"
>
> Section 3468, R. S.: "Whenever the principal in any bond given to the United States is insolvent * * * and * * * any surety on the bond * * * pays to the United States the money due upon such bond, such surety * * * shall have the like priority for the recovery and receipt of the moneys out of the estate and effects of such insolvent or deceased principal as is secured to the United States" (2 Fed. Stat. Ann. [2nd Ed.], 216, 223, 6 U. S. Compiled Stats., p. 7420).

It is conceded by the Government that the surety who pays the money due on a bond to the United States is entitled to "the like priority" that is secured to the United States, provided the Government's debt is paid in full. The priority of the Government is defined in section 3466 as "the debts due to the United States shall be first satisfied". The word "like" has been judicially defined as "equal in quantity, quality or degree; exactly corresponding" (Badger v. Daniel, 79 N. C. 372, 387). Hence, when the surety acquires the Government's priority, the surety has exactly the same rights as the Government had. The surety stand in the shoes of the Government.

The one question involved here is, when does the Surety acquire the Government's right of priority. Section 3468 plainly says the surety is substituted into the Government's priority "whenever the Surety pays to the United States the money due on such bond". The Government contends that the priority does not arise until all the debts due the Government are paid in full.

The argument of petitioner is based entirely on the theory of common-law subrogation. It is asserted by petitioner that section 3468 is merely declaratory of the common law, that it is subject to the same limitations as exist at common law, and that one of these limitations is that the creditor to whom both the

principal and his surety are debtors, must be first paid in full before the surety is entitled to enforce his right of subrogation.

Our answer to this is contained in the very wording of the statute. Section 3468 clearly says:

> "*Whenever* * * * such surety pays to the United States the *money due upon such bond* * * * such surety shall have the like priority * * * as is secured to the United States."

Counsel for petitioner have entirely overlooked the wording of this statute. The priority arises to the surety "whenever" it pays in full "the money due upon such bond" and not when the creditor is paid in full by the surety or the insolvent.

Undoubtedly Section 3648, R. S., was enacted for a definite specific purpose and was not intended to be declaratory of the common law. Had Congress intended to make the statute declaratory of the common-law subrogation, it would not have been limited to insolvent principals. The right of subrogation arises at common law whether the principal is solvent or insolvent. The section did not attempt to cover all cases, but simply to cover the case of an insolvent principal, where a surety pays all of the money due upon the *bond* which it has executed. The statute gives the "*right of priority*" to the surety for "*the money*" paid on the surety's "*bond*".

In the case of the United States v. Heaton, 128 Fed. 414 (C. C. A., 3rd Circuit), the Court approved this language used by the Circuit Court in deciding the case below:

> "The United States has no priority against a surety, for the reason that no statute his given it such a privileged position, while it has priority against an insolvent principal for the analogous reason that Congress has seen fit so to enact. The right of a surety, after he has paid the *money due upon his bond* to the United States, to be preferred in the distribution of his insolvent principal's estate, does not depend at all upon the answer to the question whether the United States has previously had priority against the surety, *but rests solely upon the language of Section 3468, which expresses the legislative will upon the subject. It is this section that is the source of the surety's right, and I think its true construction gives priority for so much, and no more of the Government's claim as the surety may have been obliged to pay* by legal proceedings, or may have paid voluntarily, *in discharge of his obligation upon the bonds.*" (Italics are ours.)

In the case of United States v. Ryder, 110 U. S. 729, 738, 28 Lawyer's Edition 308, *l. c.* 311, the Court said that section 3468 was substantially a reproduction of the proviso of the Act to Regulate the Collection of Custom Duties, approved March 2, 1799 (1 Stat., at L., 676). The Court said:

"The only diffference between Section 3468 of the Revised Statutes and this proviso is, that the latter in terms relates to bonds given for duties, whilst thee former uses the more general terms, 'whenever the principal in any bond given to the United States is insolvent, etc.' If it was intended by Conggress to enlarge the scope of the section so as to include other bonds than those given for duties,, as seems to be the necessary inference from the language, still, it is restricted to '*bonds*'; the words are 'whenever the principal in any *bomd* given to the United States is insolvent, etc.', and any 'surety on the *bond*' pays the money due upon 'such *bond*,' such surety shall havce the like priority, etc., and may bring and maintain a suit upon '*bond*' in his own name, etc. Thiss cautious phraseology, so carefully avoiding amy general words of enlargement beyond the artiicle of 'bonds' alone, seems to imply that, in extending the peculiar privileges given to suretiess, it was only intended to do so in reference to obligations of the same general character with those referred to in the original act, that is to say, bonds conditioned for the payment of money, or, at most, to embrace, besides, those conditioned for the performance of some civil duty, such as the faithful discharge of the duties of an office, etc." (Italics are the Court's.)

In the case of Hunter v. United States, 5 Peters 173, 8 Lawyers' Edition 86, Hunter was the assignee of Archibald and Frederick Crary. Jacob Smith had,

as surety in a custom house bond, been compelled to pay to the United States, for the Crarys, the sum of $2,125.90. This payment was made in 1808. In 1809 the United States obtained judgment against Smith on another bond and Smith went into insolvency. The United States claimed priority in the Crary estate, and against the other Crary creditors, on the ground that Smith, having paid a bond to the United States, was entitled to priority over the other Crary creditors. The Supreme Court of the United States sustained the priority. See also Guarantee T. & T. Co. v. Title Guarantee & S. Co., 224 U. S. 152, 56 L. Ed. 706.

The holding of the Court is to the effect that under the statutes of the United States, the surety who pays to the United States the amount of a bond, is entitled to priority over other creditors in an insolvent estate. This is peculiarly emphasized in this case, for the reason that the Government established its claim to the assets of an insolvent estate by claiming through one who had paid to the Government the amount of the surety bond.

From the above authorities and from the express language of section 3468, it is apparent that priority arises to the surety when the surety pays "*the money due upon such bond.*" The statute does not provide that priority shall arise to the surety when the surety has paid *all the claims of the Government* against a bankrupt or insolvent estate. Had Congress intended that the United States should be paid in full for *all*

*claims* which it had against a bankrupt or an insolvent, before a surety was entitled to priority after paying the full amount of its bond, suitable wording could have been used to express this thought.

In this connection, we call the Court's attention to the fact that in section 3466, the words used are "*all debts due*" and "*the debts due* to the United States," but the words used in section 3468 are, "such surety pays to the United States *the money due upon such bond*" and "such surety shall have the like priority for the recovery and receipt of *the moneys* out of the estate and effects of such insolvent" and the surety "may bring and maintain a suit upon the bond * * * for the recovery of *all moneys paid* thereon". Under section 3468, the surety pays *the moneys* due on the bond and is given the like priority to the United States to recover *the moneys* paid on the bond and expressly states that the surety may recover "*all moneys paid thereon*"; the words "*all moneys*" means "any moneys" or "whatever moneys," or, as held by the Supreme Court in United States v. Heaton, *supra*, "Its true construction gives priority for so much, and no more, of the Government's claim as the surety may have been obliged to pay by legal proceedings or may have voluntarily paid, in discharge of his obligations upon his bond."

The Supreme Court stated in United States v.

Ryder, *supra*, that the wording of the statute is "cautious phraseology." Congress, in other words, not only meant what it said, but said what it meant. The Government in its brief seeks to insert an exception in this statute and such an exception as is in contradiction of the express phraseology so "cautiously" used. Had Congress intended an exception, it could have easily added this proviso, "provided that the United States has no claim against the insolvent estate", or the wording of the statute itself could have been changed, so that the priority of the surety would not arise on its paying "the moneys due on such bond," but on its paying "all debts due to the United States from such insolvent principal".

In this connection Judge Carland said in the opinion of the Circuit Court of Appeals in this case (Rec., pp. 47, 48):

> "There is no question as to the meaning of Sec. 3466. In the cases specified in said section the United States has beyond question undoubted priority. When we come to section 3468 it is claimed by counsel for the United States that it must be so construed as to be of no force or effect except in cases where the United States has no claim whatever to be satisfied, and it appearing in the present case that the United States has a claim against the estate of the bankrupt, said section is inoperative. The ground of this contention is that the priority granted by sec-

tion 3466 still attaches to the claim of the United States even as against the claims of respondent, and that no priority exists in favor of respondent until the claim of the United States is full paid. *If this contention is sound we must read into section* 3468 *a proviso at the end of the last clause but one of the section, reading as follows, 'provided that said United States has no claim against the insolvent estate.' We do not have any authority to interpolate such a proviso.* We are of the opinion that while the general priority of the United States is undoubted, it is within the power of Congress to qualify or limit this priority, and that by the enactment of section 3468 it has been provided that in the cases mentioned in said section the priority of the United States has been transferred to a surety who has paid the penalty of a bond in full, notwithstanding the latter still has a claim against the insolvent. It is claimed by counsel for the United States that the surety in a case like the one at bar has no priority unless he pays all of the debt or debts due from the bankrupt to the United States. The section which we are endeavoring to construe does not provide that the surety shall pay all the debt or debts due from the bankrupt estate to the United States, but only the money due upon such bond, and it is conceded that the respondent did this. It paid all the debt for which it was obligated as surety. *If it should pay any more it would be a mere volunteer and not entitled to the right of subrogation as to the excess.* It is not material if the contention of

> counsel for the United States is right whether the claim of the United States arises out of the same transaction as that of respondent or not." (Italics are ours.)

The surety bases its right entirely upon that statute, and under it the surety is entitled to the same priority as the United States Government is, in an insolvent estate, *when the money due upon a bond is paid.*

In the releases and receipts signed by the United States at the time it was paid in full the amounts of the bonds, provide as follows:

> "This release and receipt is in full payment and satisfaction of all claims whatsoever on said *bond*, etc."

The Government having been paid in full by the surety company, the surety is entitled to the same priority that the Government has in the insolvent estate.

The authorities cited by opposing counsel are not in point. They are cases arising out of subrogation at common law, and not under Section 3468, R. S. Section 3468 was not intended to cover all the various situations arising in common-law subrogation. The purpose of the statute is clearly limited to an insolvent estate and to payments made by sureties on Government bonds, and awards priority where the surety

pays the full amount of the *bond*. There is no requirement under the statute that the surety shall pay *all the debts* owing by an insolvent estate to the Government, before the surety is entitled to priority.

We have read carefully the decisions cited in the brief of petitioner. These cases do not hold that the surety company is not entitled to priority where the surety has paid the full amount of the *bond* to the Government. Only one of the cases involve Government bonds, and in this case the Government was paid in full of its debt and the surety had also discharged the full amount of the bond. There is no case cited by the Government in their brief where a surety on a Government bond has paid the full amount of the bond, and the Government had not been paid in full of its debt, and these are the facts in the case at bar.

The reference to section 3468 in the case of Robertson v. Trigg's Administrator, 32 Grattan 76, is wholly *obiter*, for no claim of a surety was sought under section 3468.

In the cases of United States Fidelity and Guaranty Co. v. United States Bank and Trust Co., 228 Fed. 448, and Columbia Fidelity and Trust Company v. Kentucky Union Railway Co., 60 Fed. 794, the Court's decisions are based entirely on common-law subrogation and not upon section 3468, no Federal bond was involved and the Federal statute is not even mentioned in the opinions.

The Government's brief contends that the prerogative of sovereignty as to priority of debts to it, is such that it cannot be taken away except by express language. We contend express language has been used in Sec. 3468 sufficient to give to the surety the right of priority, when it has paid the *bond* in full. The case of Guarantee T. & T. Co. v. Title Guarantee & S. Co., 224 U. S. 152, is directly in point and sustains our position.

When the statute was enacted, the common law of subrogation was well understood and the prerogative of the Government to priority was also well understood. Having both of these principles in mind, Congress of the United States provided in clear and unambiguous language, that "whenever such surety pays to the United States *the money due upon such bond*, such surety shall have like priority for the recovery of *the moneys*."

We do not know how the idea of priority of the surety could have been more clearly expressed. The meaning of Sec. 3468 is shown in the quotations above set forth, from the cases of the United States v. Heaton, 128 Fed. 414, *l. c.* 417 (C. C. A., 3rd Cir.), and United States v. Ryder, 110 U. S. 729, 28 Lawyer's Edition 308, *l. c.* 311.

The opinion of the Circuit Court of Appeals (Rec., p. 48) says on this subject:

> "It is contended and it is no doubt the law that the priority of the sovereign exists in full force

and v[illegible]r unless qualified by express words. But *we have express words in Sec.* 3468. *We think that Secs.* 3466 *and* 3468 *should be construed together so as to give both force and effect, the United States retaining its priority as to the balance of its claims against the bankrupt estate and the respondent standing on a level with them as to its claim.* No case has been cited nor have we found one deciding the question involved. The cases cited simply establish the proposition that where the title of the United States and the citizen concur, the title of the United States except so far as the Legislature has thought fit to interfere shall be preferred, and that where the principal in any bond given to the United States is insolvent and any surety on the bond pays to the United States the money due upon such bond, such surety shall have the like priority for the recovery and receipt of the moneys out of the estate and effects of such insolvent as is secured to the United States. These rights are all given by the sections quoted and citation of other authority is unnecessary. *Respondent's rights must be determined by Sec.* 3468. *What its rights would be under the equitable doctrine of subrogation is not involved. The unreasonableness of the contention of counsel of the United States is made to appear when we consider a case where different bonds have been given by an insolvent to the United States with different sureties. One surety pays the full penalty of the bond on which he is liable, but he can have no priority until he has paid all the other bonds on which he is not liable.*" (Italics are ours.)

The Government's brief contends that if priority is allowed to the surety in this case, the Government

will lose some money. The surety in this case declines to assume the responsibility of the Government's losing the money. The surety has paid in full the bonds executed to the Government, and, as stated by the District Court in deciding this case, the bonds were "paid promptly."

The Government could have very easily secured payment of its loss in full by requiring a larger bond. The Government itself fixed the size of the bond; the surety company had no decision in the matter. The bond was arranged between the Government and the contractor. Congress evidently presumed that the officers of the Government would ask for a bond that would fully protect it; hence provided that when the bond was paid in full, the surety's priority was substituted for the priority of the Government.

There is no way to protect the Government if it insists on procuring such a small bond. If the Government had only required a $100.00 bond for a $3,000.00 contract, the Government would simply be running a chance in having the contractor fail and receiving only $100.00 from the surety.

The Government contends that if it had chosen to file its claim in bankruptcy for the full amount of its loss, and had been paid such an amount as it could have secured as a preferred claimant, it could have then proceeded on the bonds in question, and the surety company would have no defense.

There are two conclusive answers to this contention. First: No such case is presented by the record. The surety company paid in full the amount of the bonds and the Government receipted for the money in full and afterwards the Government proceeded against the bankrupt's estate. The Government having proceeded against the surety company first on the bonds, the surety company is entitled to the same priority as the Government against the insolvent estate. Second: Even if the Government had proceeded against the insolvent estate before proceeding against the surety, the surety could and would have protected its priority by tendering to the United States the amount of the bonds, and a refusal by the Government to accept the tender would have released the surety.

This not only destroys the argument of the Government that it could have secured the assets of the bankrupt estate and then have proceeded against the surety, but shows definitely that the proper construction of section 3468, giving the surety "like priority" with the Government, is fully protected, in all events, and that the construction contended for by us is the correct one.

The Government contends that under its construction of section 3468, the United States should receive the entire amount of the assets of the estate of the bankrupt mining company, leaving nothing for the

surety company. The position of the Government is, therefore, that the proper construction of section 3468 is entirely dependent upon the amount of the assets of the bankrupt estate. Our contention is that the meaning of the statute is not dependent upon the amount of the assets of the bankrupt estate, and that the words "like priority" mean that the surety has the same priority of the Government itself.

It would frequently be impossible to tell until after the time for filing the claims had expired whether or not there would be enough money to pay the Government's claims in full and still give the Surety Company a sufficient dividend to reimburse it.

The construction which the Government places upon section 3468 is apparently this: If the bankrupt estate has sufficient to pay the United States' claim in full, after the Surety Company has paid its bond in full, then the Surety Company is entitled to "like priority", but if there is not sufficient assets to pay the Government's claim and the surety's also, then the words "like priority" have no meaning. As we view the express wording of the statute, the words "like priority" mean exactly what they say, whatever the amount of the bankrupt estate. The statute provides that the Surety Company and the United States have "like priority", so far as their participation in the bankrupt estate is concerned, "when-

ever'' the surety pays the full amount of the bond. The Surety Company and the United States must, therefore, participate *pro rata* in the assets of the bankrupt estate.

The whole argument of the Government should be addressed to the Congress and not to this Court. Section 3466 of the Revised Statutes was in effect before the enactment of section 3468. It is evident, therefore, that Congress, representing the sovereign, intended to give the surety the priority which we are contending for. If the Government thinks that Congress has overlooked the possibility of the Government's accepting bonds which are not sufficient protection of Government contracts, then this is a matter for the congress.

The learned counsel for the United States have frankly conceded that the construction contended for by them is unreasonable. They say on page 13 of their brief:

> ''It is said that this construction is unreasonable, because if so construed section 3468 confers no priority upon the surety unless he pays all of the debt or debts due from the bankrupt to the United States, and if he pays more than the amount he is obligated to pay he is a mere volunteer and not entitled to subrogation as to the excess.
>
> ''That this is the consequence of adopting the Government's contention is true.''

The able opinion of the Circuit Court of Appeals also finds this fatal objection of unreasonableness in the contention of the Government (Rec., p. 48). It is, of course, a cardinal rule of statutory construction that the courts will not give a statute an unreasonable construction when a reasonable construction is possible. In the case of Knowlton v. Moore, 178 U. S. 41, 77, 44 L. Ed. 969, 984, the Court said:

> "We are therefore bound to give heed to the rule that, where a particular construction of a statute will occasion great inconvenience or produce inequality and injustice, that view is to be avoided if another and more reasonable interpretation is present in the statute" (citing cases).

The brief of petitioner (Rec., pp. 10, 11) calls attention to the fact that Section 3466 and Section 3468 were both re-enacted parts of the Act of March 2nd, 1799. That is true and significant. Sections 3466 and 3684 were at one time one statute, and section 3468 was a proviso or exception to section 3466. This statute was subsequently resolved into two parts. This shows the clear intention of Congress was to put a limitation on the rights of the Government mentioned in the first part of the statute (now section 3466) by adding the proviso (now section 3468). Judge Lurton, in Deitch v. Staub, 115 Fed. 309, 314 (C. C. A., 6th Circuit), says:

> "The primary and usual office of a proviso is to except something out of a statute which would otherwise be within it. Its use is to take special instances out of a general class" (citing Sutherland Statutory Construction, Sections 222, 223; Gibbons v. Ogden, 9 Wheat 191, 61 L. Ed. 23).

In the case of Voorhees v. Jackson, 10 Peters 449, 471, 9 L. Ed. 490, 499, the Court said:

> "The first part of this propostion is the true meaning of the law of Ohio; the various acts required to be done previous to a sale are prescribed by a proviso, which in deeds and laws is a limitation or exception to a grant made or authority conferred; the effect of which is to declare that the one shall not operate, or the other be exercised, unless in the case provided."

The history of section 3468 shows that its purpose was to carve out of the general right of priority of the Government an exception in favor of a surety. The exception is fully and accurately described in express terms to arise "whenever the surety pays to the United States the money due on such bond". The statute does not describe the exception as dependent upon the payment of all debts due by the bankrupt to the United States. Sections 3466 and 3468 are perfectly consistent, and the intention of Congress to declare by proviso the substitution of the surety in the

place of the Government as to the priority is manifest. The fact that the priority of the Government becomes the priority of the surety when the bond is fully paid negatives the idea of the petitioner that the priority accrues to the surety only when all the debts to the Government are paid. *Expressio unius exclusio alterius.*

## CONCLUSION.

We may summarize and restate in another form our argument, as follows:

(1) The Government concedes that the "like priority" to which the surety is entitled is the identical priority to which the Government itself is entitled. The only question is, does the priority of the Government become the priority of the surety *when* the full amount of the bond is paid, or *only when* all the debts accruing to the United States of the bankrupt are paid?

(2) The express words of Section 3468, R. S., give to the surety, when it pays the "money due on the bond" to the United States, "a like priority" to the United States.

(3) Section 3468 does not state that the "like priority" does not arise unless and until the surety pays *more than* the amount of the bond.

(4) Nor does section 3468 require the surety com-

pany to pay in full *all the debts* due the United States by the insolvent estate before the priority of the United States becomes the priority of the surety.

(5) Whether the United States has priority over other creditors under section 3466, or under the common law, or both, is immaterial, because under section 3468 the surety has "the like priority" to the United States for the "money paid on the bond".

(6) The construction of the statutes contended for by the Government is unreasonable. If the surety paid any more than the full penalty of the bond it would be a mere volunteer as to the excess and would not be entitled to subrogation as to such excess.

(7) That the contention of the Government is further unreasonable can be readily seen when different bonds have been given by an insolvent to the United States and one surety pays the full penalty of his bond on which he is liable. Under the Government's contention he must pay all the other bonds on which he is not liable to secure the "like priority" of the United States.

(8) The construction of the Government is unreasonable in that the meaning of the statute, if the Government's contention is correct, is dependent upon the amount of the assets of the bankrupt estate; *e. g.*, if the United States has an unpaid claim against the estate, section 3468 is inoperative, and if the bankrupt's assets are sufficient to pay the claim

of the United States and the claim of the surety also, the surety is entitled to "like priority", but if the assets are insufficient to pay both the United States and the surety, then "like priority" has no meaning. We contend that sections 3466 and 3468 should be construed together so as to give both force and effect, the United States retaining its priority as to the balance of its claims against the bankrupt's estate and the surety standing on the level with the United States as to its claim, *i. e.*, given "the like priority as is secured to the United States".

(9) The history of sections 3466 and 3468 shows that section 3468 was a proviso to section 3466 and intended to carve out an exception for the benefit of the surety who has paid its bond in full.

(10) When section 3468 was enacted, the prerogative of the Government and the common-law subrogation were well understood. Having both these rules in mind, Congress provided in clear and unambiguous terms that the priority of the Government shifts to the surety when the surety pays the money due on the bond and not when the Government is paid in full.

(11) Under the rule of *expressio unius exclusio alterius* the surety is entitled to the Government's priority when the bond is paid and not when the Government is paid in full.

(12) The language of the courts in discussing these

sections sustain the views of the Referee, the District Court and Court of Appeals, and there are no decisions to the contrary.

(13) The construction contended for by us is fair, reasonable and just.

(14) The United States could have had all of its debts paid in full by requiring a larger bond. The Government fixed the size of the bond and is alone responsible for any loss to it. The surety has paid in full.

(15) The like priority of the surety is protected in all events; for, had the United States first filed its claim against the bankrupt estate before proceeding against the surety, the surety could have tendered the amount of the bond, and a refusal of the United States to accept would have released the surety.

We can come to no other conclusion than the decisions below are correct, and the petition herein should be denied.

Respectfully submitted,

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Nos. [redacted]

# In the Supreme Court of the United States

OCTOBER TERM, 1919.

THE UNITED STATES, PETITIONER,

v.

NATIONAL SURETY COMPANY.

*ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT.*

MOTION OF THE UNITED STATES TO ADVANCE.

WASHINGTON: GOVERNMENT PRINTING OFFICE: 1920

# In the Supreme Court of the United States.

OCTOBER TERM, 1919.

THE UNITED STATES, PETITIONER,
*v.*
NATIONAL SURETY COMPANY.
Nos. 779 and 780.

*ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT.*

**MOTION BY THE UNITED STATES TO ADVANCE.**

Comes now the Solicitor General, and respectfully moves that the above-entitled cases, in which writs of certiorari were granted on April 19th last, be advanced for early hearing during the October, 1920, term of this court.

The question involved herein is whether a surety company which has paid to the United States the full amount of its bond, which, however, is less than the amount due the Government from the principal, a bankrupt, is entitled to share *pro rata* with it (the United States) in the distribution of the assets of the bankrupt debtor, or whether the claim of the United States is superior and entitled to priority of payment. The decision of this question is dependent upon the construction given Revised Statutes, sections 3466

(Comp. Stat., 1916, sec. 6372) and 3468 (Comp. Stat., 1916, sec. 6374)—the former section providing that debts due the United States shall be first satisfied out of the insolvent's estate; the latter providing that when a surety has paid to the United States the amount due upon the bond of his principal, an insolvent, he shall have the "like priority" secured to the Government for the recovery and receipt of said amount out of the estate and effects of such insolvent.

Owing to the large number of contracts into which the Government is daily entering with private parties for which surety bonds are given to secure the faithful performance thereof, the question presented herein will undoubtedly arise very frequently in the future, and its correct settlement is of the greatest importance to the public business. It is requested, therefore, that an early hearing be had in these cases.

Counsel for the respondent concur in this request for advancement.

ALEX. C. KING,
*Solicitor General.*

MAY, 1920.

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